

Price protection becomes costlier



Cotton Outlook

By JOHN OTTE

Key Points

- Commodity speculative activities hike cotton price volatility.
- Volatility makes managing cotton price risk more complex and expensive.
- Cotton prices need to rise to keep other crops from robbing acres in 2009.

SURGING commodity prices in response to surging energy demand and global economic growth are rewriting the cotton marketing play-book.

The development of more speculative trading activity with relaxed trading parameters compared to the past make the market more volatile in both the short and longer run.

“Price risk management has become complex and more expensive,” explains Carl Anderson, Texas A&M University economist. Option spread strategies face explosive price changes that growers must consider. Such strategies involve selling one option to hold down cost of getting price protection benefits from buying another option.

Delivery aid

The cotton industry is moving toward being able to effectively deliver cotton on futures contracts. Cotton certified for delivery now stands at a record, exceeding 1.5 million bales.

“Using cash deliveries on futures contracts to encourage convergence between futures price and cash price is desirable to regain using futures prices to discover cotton prices,” says Anderson.

“Producers need to evaluate their pricing alternatives in light of the lowest cost and risk of setting a selling price. The role of large cotton marketing associations, electronic markets and use of USDA Commodity Credit Corporation loans are major pricing considerations,” he adds.

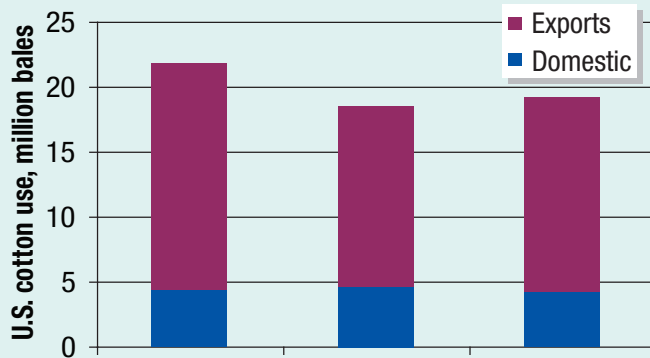
Floods overwhelm fundamentals

Supplies of nearly all commodities are tightening. Even cotton will tighten next year. Unfortunately, 2007-crop cotton carry-over stocks are large. Big immediate supplies limit buoyancy of near-term cotton rallies.

Floodwaters inundating the Corn Belt will trim 2008 grain and oilseed crops. Prices for those crops advanced sharply to ration demand. Corn, for example, needs to find a price that will entice livestock producers to feed about a billion bushels fewer of 2008-crop corn than the roughly 6.1 billion bushels of 2007-crop corn going to livestock.

Higher grain and oilseed prices mean those crops will be looking to attract more acres in 2009. Cotton prices need to advance high enough to entice cotton growers to plant enough acreage next year to meet cotton consumption for the 2009-10 marketing year. Not knowing where grain and oilseed prices will stabilize makes projecting how high 2009-crop cotton futures need to rise to protect acreage extremely challenging.

Projected 2008 cotton use up from 2007 but well below early projections for 2007



SOURCE: USDA WORLD AGRICULTURAL OUTLOOK BOARD



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